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NYC urges smaller funds to follow its lead on ESG in real estate

Trustees for the $193.5bn retirement system said they hoped to blaze a trail for smaller pension funds to follow.

Dietrich Knauth | 15 Mar 2018

Trustees for the **New York City Pension Funds** urged institutional investors around the country to take up policies that pressure real estate and infrastructure managers to pay more attention to ESG concerns like worker safety, wages and benefits, in a discussion at the **Council of Institutional Investors**' spring conference in Washington, D.C., on March 12.

The city's five pension funds, which collectively manage $193.5bn in assets, adopted responsible contractor policies (RCP) in May and June of 2017, and trustee representatives **Susannah Vickers** and **David Katzman** said that the policies provide a good pressure point for engaging managers on environmental, social and governance concerns.

Vickers, who is the Executive Director for Pensions at NYC's *Bureau of Asset Management*, as well as the NYC Comptroller's representative on four of the five pension boards, said that the city has invested in six or seven real

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estate projects since the policies went into effect. None of the managers had any problems agreeing to the city's wage, safety, and benefits policies, she said.

"Many of the big managers are relying more and more on institutional investors to raise these huge funds, to do the mega deals that they're doing in private real estate, private infrastructure, private equity," Vickers said. "They really need us as clients, and I think it's harder for them to put the deals together that they want to do and be the big players that they want to be without institutional dollars. So when we create a policy, they sort of have to listen."

The policy creates an avenue for dialogue, and forces managers to have a better idea of what's going on on the ground, she added. It also helps clarify the pension systems' goals for consultants, who often include ESG criteria in their due diligence screening of potential managers.

"The contracts with our consultants come up from time to time, and we can change our requirements, and ask them to include RCP in their database, for example," Vickers said. "Everybody talks about 'ESG' and sometimes the 'S' gets lost in the governance and environmental work that's being done, because I think it's a lot harder and there are so many other stakeholders."

The pension funds' engagement has helped secure a union contract for Teamsters parking valets working at the Hard Rock Hotel and Casino, who received $2 more per hour as well as medical and pension benefits, according to Katzman, who is the **Transport Workers Union**'s representative on the **New York City Employees Retirement System** board. **Brookfield Asset Management**, which acquired the hotel in 2011, was willing to listen because NYCERS is the kind of investor they can build long-term plans around, Katzman said.

"This particular manager was sensitive to our concerns on this matter, because they wanted a lot of money from us," Katzman said. "And not just this time – because they know and we know that in two or three years they will be back for another pot of money, and it's going to keep on going like that. And this is the one power that potential limited partners have over the

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[general partner]. A money-raising process is arduous, time-consuming and, for them, money-consuming. And there's nothing like LPs that they can do business with on a regular basis."

While the NYC pension systems have the advantage of size, Katzman and Vickers both said that they hoped smaller funds could follow in their footsteps to create a new standard for engagement with real estate managers.

"It is my hope that if large systems can have strong responsible contractor policies, then it will make it possible for anyone who's considering becoming an LP to be able to ride along," Katzman said.

Smaller funds could also learn from NYC's lessons in making sure that policies get buy-in at all levels, from boards to investment staff to managers soliciting real estate funding.

"I can imagine, for smaller funds, the thought of instituting something that managers might feel to be unreasonable would be a little bit scary, because they would be afraid of getting boxed out of various investments," Vickers said. "That's why we did a lot of up front work to make sure that our investment staff was on board and part of that was actually having them bring it to their managers and get feedback from their managers."

Real estate investing comes with a number of risks that can be mitigated by responsible contractor policies, including risks related to worker deaths and injuries, litigation costs, work stoppage and delays, and headline risks – particularly in a high-risk high-reward market like New York City, the panelists said. As examples, they mentioned lawsuits and media attention devoted to sexual harassment of female construction workers at a Hudson Yards development project. The headline risk is just as acute in the case of construction worker deaths, of which there were 50 in the last three years, according to the panelists.

"Picture the NY Post headline: 'Pension funds profit from death of construction worker.'" Katzman said. "The NY Post is not particularly enamored of pension funds or of construction workers, but they would run

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that headline in a moment. This is to exemplify the reputational risk the systems face in not having an adequate responsible contractor policy."

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